National Cleveland Corporatian

Cleveland, Ohio

1968
ANNUAL
REPORT

National Tool Company

Atom-Steel Company

11200 MADISON AVENUE • CLEVELAND, OHIO • 44102

NATIONAL CLEVELAND CORPORATION

NATIONAL TOOL DIVISION

CUTTING TOOLS

Hobs

Shaper Cutters

Shaving Cutters

Master Gears

Milling Cutters

Broaches

Boring Tools

Form Tools

ATOM STEEL DIVISION SERVICES

Stress Relieving

- Ordnance Parts
- Aircraft Parts
- Springs
- Automotive Parts

Shot Peening

Sand Blasting

Heat Treating

MACHINE TOOLS—KLINGELNBERG

Gear Hobbing—Spiral Bevel Gear Machine

Twin Head—Straight Bevel Gear Machine

Hydraulic Hardening Machine

Bevel Gear Lapping Machine

Bevel Gear Running Tester

Bevel Gear Noise Tester

Hob Sharpening Machine

Hob Face Tester

Automatic Worm Grinder

Worm Tester

Worm Drive Tester

Hob Profiling Machine

Hob Testing Machine

Universal Gear Tester

Involute and Helix Tester

FINANCIAL HIGHLIGHTS — 1968

	1968	1967
Net sales	$4,487,609	$4,388,677
Net profit	$ 166,497	$ 280,308
Shares authorized	1,500,000	1,500,000
Shares issued and outstanding	754,047	740,622
6¼ Subordinated Debentures converted @ $3.04 per share	15	15
Earnings per share	$.22	$.43
Earnings per share after full conversion and exercise of warrants	$.21	$.36
Total shareholders' equity	$1,254,489	$1,056,029
Indebtedness due beyond one year	$ 293,886	$ 318,699
Working capital	$ 679,199	$ 640,322

March 18, 1969

President's Letter to Shareholders of National Cleveland Corporation:

During 1968 sales rose moderately in a continuation of the generally upward pattern of the past five years. Profits, on the other hand, fell approximately forty percent from $280,308 in 1967 to $166,497. Earnings were adversely affected by (1) a decline in tool sales of higher margin lines, (2) a general shortening in delivery lead times as an overall industry practice, (3) a work stoppage at the Atom-Steel Division over the year-end, and (4) increases in taxes, employee fringe benefits and pension fund payments.

National Tool Division, which primarily serves capital good industries, experienced a gain of approximately ten per cent in sales over 1967. This reflected the strengthening of our sales organization and the addition of a new long-life shaper cutter to the line. The early reception given to this new shaper cutter has been so favorable that we anticipate it will produce important additional sales volume. The backlog of orders in the National Tool Division was up twenty-six per cent over year-end 1967 but will probably be reduced due to customer practices of shorter lead times and lower inventories.

Sales as United States' representative for the fine line of machine tools and cutting tools manufactured by W. Ferd Klingelnberg Sohne of Remscheid, Germany, showed a substantial increase over 1967. Leading customers have compared the performance of Klingelnberg products against other tools and equipment. It is a pleasure to report that the findings of two large American manufacturers based upon their statistical analyses and control studies indicate a superior rating for Klingelnberg machine tools. The result has been the receipt of sizable orders for shipment commencing in mid-1969. With such recognition and increasing acceptance by industry, our Klingelnberg sales during 1969 should expand further.

The ultrasonic treatment by the Atom-Steel Division of tools manufactured by the Tool Division increases the life of the tools and makes them more attractive to our customers. In addition, Atom-Steel's shot peening, shot blasting and stress relieving operations were strong during the first three quarters of the year. The work stoppage, already mentioned, which commenced December 9, 1968 and ran through the end of the year, reduced the contribution to profit which would otherwise have been expected from this Division.

In operations, a number of steps have been taken to effect economies in both machining and heat treating. In marketing, computerized sales analysis, new distribution arrangements and more aggressive advertising and promotion are some of the steps adopted to strengthen our total marketing impact.

As to the future, opportunities for building upon the excellent reputation of our product lines are available. To take advantage of these opportunities, a major capital investment in production machinery is needed. Your management has devoted substantial time and effort to the formulation of a clearly defined program for such an investment, holding the firm conviction that it is essential to the welfare of the Company and the best interests of the individual shareholders.

We are grateful to our customers, our employees, and our suppliers for their support during 1968 and likewise express our appreciation to our shareholders for their confidence and loyalty.

Richard M. Bourne

RICHARD M. BOURNE
Chairman of the Board

K. E. Barker

K. E. BARKER
President

National Cleveland Corporation

(AN OHIO CORPORATION)

Balance Sheets, December 31, 1968 and 1967

ASSETS

	1968	1967
CURRENT ASSETS:		
Cash	$ 181,886	$ 174,036
Certificate of deposit		51,000
Notes and accounts receivable:		
Trade (less allowance for doubtful accounts of $87,205 in 1968 and $100,787 in 1967)	389,389	431,642
Other	5,462	14,250
Inventories, at the lower of cost (first-in, first-out basis) or market:		
Finished goods and work in process	414,381	294,138
Raw materials and supplies	48,857	69,302
Prepaid expenses	83,075	74,708
Total current assets	1,123,050	1,109,076
PROPERTY, PLANT AND EQUIPMENT, at cost (Note 1):		
Land	39,917	39,917
Buildings	529,117	530,322
Machinery and equipment	2,419,932	2,260,102
	2,988,966	2,830,341
Less accumulated depreciation	2,143,178	2,126,664
	845,788	703,677
OTHER ASSETS:		
Unamortized debenture expense	5,999	10,323
Insurance deposits	9,554	9,554
Other	7,835	10,852
	23,388	30,729
Total assets	$1,992,226	$1,843,482

The accompanying notes are an integral part of these financial statements.

National Cleveland Corporation

(AN OHIO CORPORATION)

Balance Sheets, December 31, 1968 and 1967

LIABILITIES

	1968	1967
CURRENT LIABILITIES:		
Current portion of long-term debt (Note 2):		
Bank	$ 5,481	$ 55,081
6¼% debentures	72,000	57,000
Other	35,515	23,709
Accounts payable	113,476	121,382
Accrued expenses	217,379	211,582
Total current liabilities	443,851	468,754
LONG-TERM DEBT, less current maturities (Notes 2 and 3)	293,886	318,699

Contingent liabilities and commitments (Notes 1 and 6)

SHAREHOLDERS' EQUITY

	1968	1967
Preferred shares, par value $50, authorized 50,000 shares; none issued	—	—
Common shares, par value $1, authorized 1,500,000 shares; issued and outstanding 754,047 shares in 1968 and 740,622 shares in 1967 (Note 3)	754,047	740,622
Additional capital	624,395	605,857
Accumulated deficit (Note 2)	(123,953)	(290,450)
Total shareholders' equity	1,254,489	1,056,029
Total liabilities and shareholders' equity	$1,992,226	$1,843,482

National Cleveland Corporation

Statements of Income

For the years ended December 31, 1968 and 1967

	1968	1967
NET SALES	$4,487,609	$4,388,677
Cost of sales	3,717,789	3,468,863
Gross profit	769,820	919,814
Selling, general and administrative expenses	577,773	576,084
Profit from operations	192,047	343,730
OTHER DEDUCTIONS (INCOME), NET:		
Interest and debenture expense	36,433	46,002
Other	(10,883)	17,420
	25,550	63,422
Income before federal income taxes and extraordinary item	166,497	280,308
PROVISION FOR FEDERAL INCOME TAXES	84,000	129,500
Income before extraordinary item	82,497	150,808
EXTRAORDINARY ITEM:		
Elimination of federal income tax expense resulting from available tax loss carryforward	84,000	129,500
Net income	$ 166,497	$ 280,308
EARNINGS PER SHARE OF COMMON STOCK:		
Income before extraordinary item	$.11	$.23
Extraordinary item	.11	.20
Net income	$.22	$.43
PRO FORMA — Assuming conversion of all convertible debentures and exercise of warrants:		
Income before extraordinary item	$.11	$.19
Extraordinary item	.10	.17
Net income	$.21	$.36

The accompanying notes are an integral part of these financial statements.

National Cleveland Corporation

Statements of Shareholders' Equity

For the years ended December 31, 1968 and 1967

	Common Shares	Additional Capital	Accumulated Deficit	Total
Balances, December 31, 1966	$634,194	$594,306	$(570,758)	$ 657,742
Net income for the year			280,308	280,308
104,928 shares issued for conversion of long-term obligations	104,928	10,051		114,979
1,500 shares issued under stock option plan (Note 3)	1,500	1,500		3,000
Balances, December 31, 1967 . .	740,622	605,857	(290,450)	1,056,029
Net income for the year			166,497	166,497
4,925 shares issued for conversion of long-term obligations	4,925	10,038		14,963
8,500 shares issued under stock option plan (Note 3)	8,500	8,500		17,000
Balances, December 31, 1968 . .	$754,047	$624,395	$(123,953)	$1,254,489

1. The Company has entered into agreements to lease certain machinery and equipment under terms which are essentially equivalent to a purchase. In accordance with Opinion 5 of the Accounting Principles Board such transactions are being accounted for as purchases. Included in the balance sheet at December 31, 1968 is machinery and equipment with a cost less accumulated depreciation of $219,279 which is subject to the lease/purchase obligations. The commuted value of future payments is included as a liability on the balance sheet.

A substantial portion of the lease/purchase obligations were entered into in 1968. Similar transactions in prior years were accounted for as lease transactions. To provide for consistent treatment of lease/purchase obligations, the financial statements for 1967 have been restated to reflect this change. This restatement has the effect of increasing previously reported shareholders' equity at January 1, 1967 by $14,162 and increasing previously reported net income for 1967 by $8,812.

At December 31, 1968, the Company had a commitment to lease certain machinery and equipment for an aggregate rental of $100,000 payable over a period of eight years from the date the machinery and equipment is accepted. This transaction will be treated as a purchase for financial statement purposes.

2. Long-term debt consisted of the following at December 31, 1968 and 1967:

	1968	1967
Debt payable to bank:		
6% note, final maturity December, 1968		$ 49,600
Note payable in monthly installments of $457 for principal and interest to July, 1971	$ 13,702	19,183
Machinery lease/purchase obligations	181,679	97,707
6¼% convertible subordinated debentures payable through annual sinking fund payments in ascending amounts . . .	210,000	285,000
Notes payable, other	1,501	2,999
	406,882	454,489
Amounts due within one year	112,996	135,790
	$293,886	$318,699

At December 31, 1968, the Company held $18,000 of 6¼% debentures which will be used as part payment of the sinking fund requirement of $90,000 due in 1969.

Notes to Financial Statements, Concluded

The lease obligations provide for payments including interest over a period of six to nine years from the time the related machinery is generally placed in operation. Amounts payable under these obligations are due as follows: $47,024, 1969; $39,607, 1970; $36,387, 1971; and an aggregate of $105,964, 1972 to 1976.

The debenture agreement contains restrictions relating, among other things, to the payment of cash dividends and maintenance of working capital with which the Company has complied.

3. At December 31, 1968, 69,079 common shares were reserved for conversion of the 6¼% debentures at the current conversion price of $3.04 per share.

The Company has issued and outstanding warrants for the purchase of its common shares as follows: 91,428 shares at $2.1875 per share and 61,538 shares at $1.625 per share, expiring September 25, 1971 and June 14, 1973, respectively.

At December 31, 1968, there were 15,000 common shares reserved for options to officers and key personnel. Under the Company's stock option plan, 5,000 shares at prices aggregating $14,110 were issuable under options outstanding and 10,000 shares were reserved for additional options. Options for 8,500 shares were exercised in 1968 at a total price of $17,000.

4. At December 31, 1968, the Company has charged against income in prior years provisions for certain reserves, totaling $200,000, which will be deducted from taxable income in future years.

Unused investment credits available against future federal income tax liabilities total approximately $40,000 at December 31, 1968. Such credits expire in varying amounts to December 31, 1974. Utilization of available credits prior to their expiration date is contingent on future earnings of the Company.

5. Substantially all of the employees of the Company are covered by funded pension plans which provide for defined contributions. Such contributions are sufficient in amount to provide for current service costs and amortization of past service costs over approximately 30 years. Pension costs charged to income in 1968 and 1967 amounted to $65,056 and $58,661, respectively.

During 1968, the pension plans were amended to include certain vested benefits; unfunded vested benefits amounted to approximately $610,000 at December 31, 1968. The Company's policy is to fund pension cost accrued.

6. The Company is a defendant in a pending lawsuit in which damages plus costs are alleged to have resulted by reason of a sales contract of the Company. Liability has been denied by the Company, and it is not possible now to determine what, if any, liability may be established against the Company in this case. The Company has also filed a counter claim against the plaintiff.

7. Depreciation and amortization amounted to $104,712 in 1968 and $99,760 in 1967. The Company provides for depreciation on the straight-line method for substantially all classes of plant and equipment.

Accountants' Report

To the Shareholders and Board of Directors
National Cleveland Corporation

We have examined the balance sheet of National Cleveland Corporation as of December 31, 1968 and the related statements of income and shareholders' equity for the year then ended. Our examination was made in accordance with generally accepted auditing standards, and accordingly included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances. We previously examined and reported upon the financial statements of the company for the year ended December 31, 1967; which have been restated to reflect the change described in Note 1 to the financial statements.

In our opinion, subject to the adjustment, if any, which may result from the final disposition of the lawsuit referred to in Note 6 to the financial statements, the aforementioned financial statements present fairly the financial position of National Cleveland Corporation at December 31, 1968 and 1967, and the results of operations for the years then ended, in conformity with generally accepted accounting principles applied on a consistent basis.

LYBRAND, ROSS BROS. & MONTGOMERY

Cleveland, Ohio
February 10, 1969

DIRECTORS

*KERMIT E. BARKER
WARNER B. BISHOP
*RICHARD M. BOURNE
*JAMES M. KILLPACK
*JOHN M. CAREN
JOHN D. IGOE
RICHARD F. STEVENS

*Executive Committee

OFFICERS

RICHARD M. BOURNE	*Chairman of the Board*
KERMIT E. BARKER	*President*
HERBERT L. DODSON	*Vice President-Sales and Marketing*
ANTON C. ERHARDT	*Vice President-Technical Services*
RICHARD F. STEVENS	*Secretary*
LORETTA G. MILLER	*Assistant Secretary*
JOHN H. HIGGINS	*Treasurer*

General Counsel	BAKER, HOSTETLER & PATTERSON
Registrar and Transfer Agent	THE CLEVELAND TRUST COMPANY
Independent Auditors	LYBRAND, ROSS BROS. & MONTGOMERY

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Tools
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